United States Court of Appeals

for the Second Circuit

SUPPLEMENTAL BRIEF

75-5024

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P/S

Docket No. 75-5024

HARVEY R. MILLER, as Trustee in Bankruptcy of IRA HAUPT & Co., a Limited Partnership, Bankrupt,
Plaintiff-Appellant,

against

NEW YORK PRODUCE EXCHANGE, *et al.*,
Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

SUPPLEMENTAL BRIEF OF DEFENDANTS-APPELLEES ANDERSON AND MERRILL LYNCH

BROWN, WOOD, IVEY, MITCHELL & PETTY
Attorneys for Defendants-Appellees Harry B. Anderson and Merrill Lynch, Pierce, Fenner & Smith Incorporated
One Liberty Plaza
New York, New York 10006

HENRY F. MINNEROP
DUNCAN N. DARROW
of Counsel

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This supplemental "fact" brief is submitted on behalf of defendants-appellees Harry B. Anderson ("Anderson") and Merrill Lynch, Pierce, Fenner & Smith Incorporated ("Merrill Lynch").* Its purpose is twofold: One, to correct the distortions contained in the Trustee's brief and, two, to tell accurately the story of Anderson's conduct as a director of the New York Produce Exchange and the role of his employer, Merrill Lynch, in the events of 1963.

Introduction

To accuse Anderson of bad faith or negligent conduct on the New York Produce Exchange ("Produce Exchange"), as the Trustee does, is simply outlandish. For, it was An-

* Both Anderson and Merrill Lynch fully subscribe to defendants-appellees' main brief and respectfully refer the Court to that brief for a statement of the issues and defendants-appellees' legal arguments.

derson's watchfulness which resulted in the discovery on November 14, 1963 that Allied held 90% of the entire open long position in cottonseed oil futures contracts. And, it was he who triggered the Produce Exchange's regulatory actions during the November 14 to 19 period, which culminated in the settlement of all open contracts in an attempt to save Haupt from bankruptcy. In sum, Anderson's conduct was faithful and conscientious throughout. He had no self-interest in the regulation of the Produce Exchange. His employer, Merrill Lynch, had not a farthing to gain from the alleged conspiracy to regulate the market in bad faith. If honorable men, such as Anderson, are to be encouraged to serve as directors of exchanges, spurious attacks upon their integrity cannot be condoned.

The Facts

Anderson was, in 1963, a member of the Board of the Produce Exchange (Anderson, Tr. 3173, JA 1172a). He received no compensation for his services (Anderson, Tr. 3334, JA 1270a) and none of his responsibilities related directly to the day-to-day administration of, or trading on, the Produce Exchange.*

* Anderson served on a number of committees of the Produce Exchange, dealing with the overall structure of the market. None of these committees was a "floor" committee charged with supervising trading on the floor. Thus, Anderson was on the Executive Committee of the Board (Anderson, Tr. 3172, JA 1171a) and was the chairman of the Business Conduct and Cottonseed Products Committees. (Anderson, Tr. 3173, JA 1172a). The Executive Committee did not function separately from the Board, except in emergencies. (MacDonald, Tr. 1485, JA 509a). The Business Conduct Committee functioned in a manner similar to a court, acting on complaints and was not concerned with the daily supervision of trading. (MacDonald, Tr. 1430, JA 494a; Anderson, Tr. 3303-3304, JA 1248a-1249a). The Cottonseed Products Committee dealt with such long range matters as the form and scope of the cottonseed oil futures contract and the licensing of Produce Exchange warehouses. (MacDonald, Tr.

Anderson had been active in the commodities futures field since 1947 when he joined Merrill Lynch. (Anderson, Tr. 3322, JA 1258a). In addition to being on the Board of the Produce Exchange since the late 1950's (Anderson, Tr. 3172, JA 1171a), Anderson was or had been a director of the Cotton Exchange, the Cocoa Exchange, the Metal Exchange Clearing Association and the Sugar Exchange Clearing Association (Anderson, Tr. 3323, JA 1259a).

Anderson was employed in 1963 as the director of Merrill Lynch's Commodities Division. (Anderson, Tr. 3171, JA 1170a).* His work did not take him to the floor of the Produce Exchange nor did it involve him directly with any of its other facilities. (Anderson, Tr. 3174-3175, 3199-3200, JA 1173a-1174a, 1191a-1192a). The Commodities Division was one of Merrill Lynch's "service divisions", not a "sales division". (Anderson, Tr. 3174, JA 1173a). It was responsible for providing commodities research for customers and, in addition, was staffed with specialists in various commodities. (Anderson, Tr. 3174-3175, JA 1173a-1174a).

Merrill Lynch was, at all relevant times, a registered commission merchant ("broker"), which executed orders for customers for the purchase or sale of futures contracts in cottonseed oil on the Produce Exchange and other markets. (Anderson, Tr. 3175, JA 1174a). At no time did Merrill Lynch maintain a "house account" or have a proprietary interest in *any* futures contracts traded on *any* exchange. (Anderson, Tr. 3175, JA 1174). *Merrill Lynch's sole interest was that of a broker for customers and its only*

1429, JA 493a). Finally, Anderson was "acting president" of the Produce Exchange in 1963 (Anderson, Tr. 3173, JA 1172a), a position which called upon him to preside in the event that both the president (MacDonald) and the vice-president (Vogel) were absent. (Vogel, Tr. 3916, JA 1480a). This eventuality never occurred in 1963. (Vogel, Tr. 3916, JA 1480a).

* Anderson was also a member of Merrill Lynch's board of directors and its executive committee. (Anderson, Tr. 3171-3172, JA 1170a-1171a).

compensation was derived from the commissions generated by such transactions. (Dahl, Tr. 839-841, JA 386a-388a; Anderson, Tr. 3175, JA 1174a).

Confidentiality, indeed secrecy, is a cardinal principle in commodities futures trading. (Leuthold, Tr. 262-263, JA 229a-230a; Dahl, Tr. 797-798, JA 373a-374a). This principle was acknowledged and fostered by the Commodities Exchange Act ("Act"). (Dahl, Tr. 796-798, JA 372a-374a; McMinn, Tr. 2460, JA 879a). The identity of purchasers and sellers, for example, is highly confidential information. (Dahl, Tr. 797, JA 373a; McMinn, Tr. 2445-2446, JA 871a-872a). While Merrill Lynch knew the identity of its own customers, it did *not* know the identity of the customers represented by brokers on the opposite side of its customers' transactions. (Dahl, Tr. 840-841, JA 387a-388a; Anderson, Tr. 3316, JA 1253a). All reports required to be filed by brokers, such as Merrill Lynch, with the Commodities Exchange Authority ("CEA") identified their customers by code number only. (Ellison, Tr. 483, JA 255a). The CEA, and only it, was privy to the key to the code and all information published by it protected the secrecy of the market place. (Ellison, Tr. 483, JA 255a; McMinn, Tr. 2446, JA 872a).

An appreciation of the confidential nature of commodities trading is essential to the proper resolution of this case. For it is the Trustee's claim that the Produce Exchange, including Anderson and Merrill Lynch, knew or should have known certain facts about Allied and Haupt which threatened the integrity of the cottonseed oil market, but that they did nothing about them until it was too late. Thus, accepting the Trustee's claim at face value, it would seem essential for him to show *what* any given individual defendant knew or should have known about Haupt and Allied and *when* he had or should have gained such knowledge. The Trustee has, however, ignored the confidentiality of the market and lumped together various isolated pieces

of information known separately, if at all, by some members of the market and has indiscriminately imputed this information to all defendants. He has compounded this distortion by fusing this separately held information with that gained only belatedly and by hindsight through pre-trial discovery of the confidential files of the CEA in this action. He now audaciously presents this information, complete with graphs and charts, as if it had actually been known or available, *in toto,* to all defendants in 1963 as events were taking shape. The result is a complete distortion of the facts.

The Trustee's obfuscations begin on appeal with the invention of the term "trader-regulators", a phrase purportedly descriptive of the roles and functions of all defendants. (T. Brief, p. 2). Yet, when applied to a specific defendant, this term is but a piece of legerdemain, created to suggest the existence of actual and irreconcilable conflicts of interest. Thus, Anderson, while a "regulator", in the sense that he served on the Board of the Produce Exchange, was never a "trader". (Anderson, Tr. 3172-3175, JA 1171a-1174a). As for Merrill Lynch, it was neither a "regulator" nor a "trader" at any time, but functioned solely as a broker for its customers. (Anderson, Tr. 3175, JA 1174a).*

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* Being faced with the undisputable fact that neither Anderson nor Merrill Lynch had anything to gain from regulating the market in bad faith or entering a conspiracy toward that end, the Trustee suggests that Anderson, nevertheless, abused his position to benefit Merrill Lynch customers. Thus, the Trustee argues that "Merrill Lynch seized the opportunity [during the period November 14 to 19] to assist its short customers by 'selling the market down'." (T. Brief, p. 41.) But, as is true so often, the facts simply do not support his argument. His own expert accounting witness, Joseph Ellison, testified, on cross examination, that on November 18, 1963, when the market had its steepest and only sharp decline (approximately 100 points) in the post-November 14 period, Merrill Lynch sold for customers 138 contracts *and bought 128.* (Ellison, Tr. 5217-5218, JA 1811a-1812a). Thus, Merrill Lynch customers as a whole went short only 10 contracts that day. This hardly constituted "selling the market down".

The Trustee's Brief is replete with other distortions. It falsely and repeatedly states that Merrill Lynch maintained a business relationship with DeAngelis or Allied in 1963; the Trustee's suggestion being that Merrill Lynch (and Anderson) were, therefore, fully familiar with DeAngelis' and Allied's activities and, hence, should have stopped them. See, *e.g.,* T. Brief, pp. 15-16. The contrary is a matter of record and was clearly testified to by Anderson (Tr. 3212-3213, JA 1200a-1201a) and DeAngelis (Tr. 2916, JA 1098a) and was disputed by no one.

Moreover, the Trustee repeatedly argues—without a shred of evidence to support his position—that Merrill Lynch was possessed of the same knowledge of Allied or DeAngelis as were Merrill Lynch's brokerage customers who happened to be dealing with Allied independently of Merrill Lynch. Specifically, the Trustee argues that since Merrill Lynch acted as broker for Bunge Corporation ("Bunge"), Continental Grain Company ("Continental") and many other companies, and since these companies were dealing with Allied, it, Merrill Lynch, knew not only the nature of their dealings but also the financial condition of Allied in 1963, See, *e.g.,* T. Brief, pp. 22, 27-28, 50. The undisputed evidence is that Merrill Lynch (and Anderson) were unaware of the independent business dealings of its customers with Allied—to the extent that they had any dealings with Allied—and had no reason to inquire into them. (Dahl, Tr. 840-841, JA 387a-388a; Anderson, Tr. 3316, JA 1253a).

It is of flimsy stuff such as this that the Trustee's case is fabricated. A fair reading of the record on appeal shows that, rather than deserving to be cast as villains in the Trustee's piece, Anderson and Merrill Lynch, among others, deserve high praise for their conduct.

The Pre-November 14 Period

It is the Trustee's contention that the pre-November 14 period was marked by a number of clear "warning signals" which should have been heeded by the Produce Exchange. These "warning signals" are said to have been, one, an increase in trading volume; two, an increase in the open interest; three, an increase in the concentration of the open interest; four, an increase in deliveries of the actual commodity; and, five, an increase in ex-pit transactions, (T. Brief, pp. 17-18).

Anderson, who had been in the commodities brokerage field since 1947, was aware of these indicia of increased activities on the Produce Exchange. (Anderson, Tr. 3322-3327, JA 1258a-1263a). He did not regard them, however, as "warning signals". They made good sense to him in the commercial context in which they appeared. (Anderson, Tr. 3324, JA 1260a). Thus, Anderson was aware that the volume of trading had greatly increased on all exchanges, including the Produce Exchange, where food commodities futures contracts were being traded in 1963. (Anderson, Tr. 3182-3183, 3323-3324, JA 1178a-1179a, 1259a-1260a). This general increase was due in great part to burgeoning export sales to the Soviet Union and other countries in food commodities such as wheat and corn and it was generally anticipated that other food stuffs, such as edible oils, would also experience heavy export demands. (Anderson, Tr. 3201, 3327, JA 1193a, 1263a). He was not alarmed by an increase in the open position on the Produce Exchange because that simply reflected the greater volume of trading. (Anderson, Tr. 3325, JA 1261a). Nor was he surprised to see an increase in deliveries because, as chairman of the Cottonseed Products Committee, he had witnessed a large increase in licensed warehouse space suitable for the delivery of cottonseed oil on the Produce Exchange. (Anderson,

Tr. 3325-3326, JA 1261a-1262a). Finally, the increase in licensed warehouse capacity gave commercial logic to the increase in ex-pit transactions because licensed warehouse receipts would normally be transferred in connection with deliveries on the Produce Exchange or in connection with ex-pit transactions. (Anderson, Tr. 3326, JA 1262a). Significantly, the Trustee's own expert witnesses conceded, on cross examination, that the so-called "warning signals" were, even with benefit of hindsight, ambiguous portents at best. (Leuthold, Tr. 326-328, JA 237a-239a; Dahl, Tr. 701, 711, 732-734, 815-816, JA 333a, 337a, 343a-345a, 377a-378a). Anderson was admittedly not, however, aware—prior to November 14—of any undue concentration of the open interest, either long or short. (Anderson, Tr. 3183, JA 1179a). But no one, including the CEA, published any statistics reflecting the concentration of the open interest. (Dahl, Tr. 740, 748, JA 346a, 351a; Berg, Tr. 2016, JA 704a). *Haupt, however, knew the full measure of this concentration by virtue of its dealings with Allied; for it, Haupt, carried Allied's position. Furthermore, Haupt knew the exact extent to which Allied was the cause of the other market indicia and should have understood them to be "warning signals", if indeed they were to be interpreted as such.* (Farris, Tr. 5937-5938, JA 2031a-2032a).

To Anderson and others, true danger signals were absent in the pre-November 14 period. Most significantly, there were no great price fluctuations to indicate a possibly disorderly market. (Anderson, Tr. 3201, JA 1193a). Instead, there was only a moderate upward price trend through the summer and fall of 1963 (Anderson, Tr. 3201, JA 1193a). Moreover, there was an enormous "visible supply" of cottonseed oil readily available during the fall harvest season which made a manipulation or corner most unlikely. (Anderson, Tr. 3330-3331, JA 1266a-1267a). There were no complaints from anyone. (Berg, Tr. 1993-

1998, 2027-2028, 2033, JA 687a-692a, 707a-70[illegible], 711a). The shorts were not and could not be "squeezed" and they were not "scrambling" for oil. (Anderson, Tr. 3332-3333, JA 1268a-1269a). As Anderson testified, anyone trying to squeeze the shorts "would have been drowned in oil". (Anderson, Tr. 3330-3331, JA 1266a-1267a).

Although Anderson was not alarmed by what he observed in the pre-November 14 period, he noted, with more than passing interest, the rumors circulating about Allied and DeAngelis. These rumors were, in essence, that Allied was responsible for a lot of the buying on the Produce Exchange. (Anderson, Tr. 3196-3197, 3202, JA 1188a-1189a, 1194a). He first heard these rumors when he returned from vacation in August. (Anderson, Tr. 3202, JA 1194a). While these rumors could easily be explained by the fact that Allied was considered to be the country's largest refiner and exporter of vegetable oils (Anderson, Tr. 3327, JA 1263a), Anderson's interest was, nevertheless, aroused. For, several years earlier a company, also headed by DeAngelis, had been a commodities customer of Merrill Lynch and had gone bankrupt, leaving Merrill Lynch and others "holding the bag". (Anderson, Tr. 3212-3213, JA 1200a-1201a). True, DeAngelis had subsequently paid all debts, but Merrill Lynch, consistent with the firm's general policy, had refused to do further business with DeAngelis or any of his companies, including Allied. (Anderson, Tr. 3212-3213, JA 1200a-1201a). Given this history, when rumors of heavy buying by Allied circulated in the summer of 1963, Anderson put his ear to the ground.

Anderson spoke first with Claggett, a CEA official from Washington, D.C., who was in a position to know exactly what every trader, including Allied, was doing and whether it made any commercial sense. Claggett's comments were reassuring: "Don't worry, we are watching [Allied] very closely, on a day-to-day basis, and so far as we can see

everything is all right." (Anderson, Tr. 3204, JA 1195a). Thereafter, Anderson spoke with William McGregor of the Morgan Guaranty Trust Company, whom Anderson considered to be the most knowledgeable commodities banker in New York. (Anderson, Tr. 3204, JA 1195a). McGregor told Anderson that, so far as he knew, Allied did not have any problems. One of his bank's customers was receiving good collateral from Allied in the form of American Express warehouse receipts (Anderson, Tr. 3204, JA 1195a). Anderson also spoke with William Love, chief official at Anderson, Clayton & Co., a major producer of cottonseed oil. (Tr. 3205, JA 1196a). Love told Anderson that his company's experience with Allied had been satisfactory (Anderson, Tr. 3205, JA 1196a). Richard Forti, an executive at Bunge, a large exporter of vegetable oils, was yet another person whom Anderson consulted. Forti told Anderson that there were always rumors about DeAngelis, almost all of them untrue, and that he, Forti, felt that DeAngelis knew what he was doing and was not on "thin ice." (Anderson, Tr. 3205a, JA 1196a). Finally, in connection with a routine request from a foreign customer of Merrill Lynch for a credit rating on Allied, Anderson instructed the Merrill Lynch Credit Department to investigate Allied's credit rating. The Credit Department reported that all banks which were dealing with Allied had given favorable credit reports. (Anderson, Tr. 3205, JA 1196a).

Approximately at this point during Anderson's informal inquiries, it was announced that the Soviet Union had concluded large wheat purchases in Canada. (Anderson, Tr. 3201, JA 1193a). This was the first time that the Soviets had entered the North American market in any major way. (Leuthold, Tr. 321, JA 234a). Their purchases were thought to be the result of adverse weather conditions in the Soviet Union. (Anderson, Tr. 3209, JA 1197a). It was believed

that Soviet vegetable oil purchases would also be forthcoming because of similar crop failures. Given the announcement of consummated Soviet wheat purchases and the expectation of future Soviet oil purchases, Anderson thought he had found the reason behind Allied's rumored buying on the Produce Exchange: Allied either already had or expected to obtain Soviet orders and his futures buying was a hedge for such Soviet orders. (Anderson, Tr. 3327, JA 1263a). Allied was, of course, known to be the largest exporter of all types of vegetable oils (MacDonald, Tr. 1479, JA 506a; Anderson, Tr. 3201, 3327, JA 1193a, 1263a) and had previously filled large orders placed by Spain and Yugoslavia. (DeAngelis, Tr. 2787, 2791, 2929, JA 1046a, 1050a, 1103a). Consequently, Anderson's concern about Allied was temporarily allayed. (Anderson, Tr. 3327, JA 1263a).

However, when by the beginning of November, no vegetable oil exports to the Soviets had materialized, Anderson's concern resurfaced, resulting in his now intensified investigation. (Anderson, Tr. 3210, 3212, 3214, JA 1198a, 1200a, 1202a). Using the expertise of James McHale, Merrill Lynch's fats and oils specialist in Chicago, Anderson came to the tentative conclusion that oil exports to Russia were unlikely to occur in 1963. (Anderson, Tr. 3209, JA 1197a). McHale had made a study which revealed that adverse weather in the Soviet Union had been confined mainly to the grain growing areas. (Anderson, Tr. 3209, JA 1197a). Given this finding, Anderson was at a loss to explain Allied's rumored buying on the Produce Exchange. (Anderson, Tr. 3210, 3214, JA 1198a, 1202a). Accordingly, Anderson instructed McHale to try to estimate Allied's total open position in cottonseed oil and soybean oil futures contracts to see whether the rumors of Allied's buying had any substance. (Anderson, Tr. 3210, JA 1198a). At about

the same time, he also instructed the Merrill Lynch Credit Department to conduct another credit check of Allied. (Anderson, Tr. 3210, JA 1198a).

On November 13, McHale reported back to Anderson, estimating that Allied's open position to be a startling 50% in both markets. (Anderson, Tr. 3210, JA 1198a). Upon receiving this estimate, Anderson first tried to reach Donald MacDonald, the President of the Produce Exchange, who was, however, absent from his office at the time. (Anderson, Tr. 3219, JA 1203a). Anderson then called Walter Klein, a fellow Board and Executive Committee member at the Produce Exchange, and proceeded immediately to his office, which was but a block away. (Anderson, Tr. 3219, JA 1203a). There, Anderson told Klein and Forti,* who was also present in Klein's office, that McHale thought a Soviet oil deal was improbable and, further, that McHale estimated that Allied held approximately 50% of the long position in both markets. (Anderson, Tr. 3221, JA 1205a). Klein expressed disbelief at the size of the estimate (Anderson, Tr. 3221, JA 1205a), but both he and Anderson urged that McHale's estimate be verified, since, according to Anderson, "unlikely as it seemed", it might be that a "squeeze" was developing despite the fact that there was an enormous "visible supply" of oil. (Anderson, Tr. 3330-3331, JA 1266a-1267a). A call was placed to Carl Berg, Managing Director of the Produce Exchange. Anderson informed Berg of McHale's estimate and asked Berg to check immediately with the CEA. (Anderson, Tr. 3221, JA 1205a). Then, Anderson, Klein, and Forti went to the Produce Exchange, where Berg told them that he had already spoken with Robin-

* Richard Forti was a vice-president of Bunge and also a member of the Produce Exchange's Cottonseed Products Committee. (DeAngelis, Tr. 2772, JA 1032a; Anderson, Tr. 3195, 3221, JA 1187a, 1205a).

son of the CEA, who was clearing the Produce Exchange's request with Alex Caldwell, the head of the CEA, in Washington. (Anderson, Tr. 3223, JA 1207a). After a few moments, Robinson called back to inform Berg that the requested information would be made available to him on a confidential basis the following morning. (Anderson, Tr. 3224, JA 1208a). Thereupon, Anderson, Klein and Forti departed. (Anderson, Tr. 3224, JA 1208a). It being late in the day, Anderson went straight home. (Anderson, Tr. 3224, JA 1208a).

The November 14-20 Period

Thursday, November 14

The next morning, Thursday, November 14, 1963, Anderson, upon arriving at his office, immediately telephoned Berg at the Produce Exchange (Anderson, Tr. 3224-3227, JA 1208a-1211a):

> A. I said, "Bob, am I right; is it 50 per cent?" And he said, "No, it is 90 per cent."
>
> Q. Was that the entire conversation?
>
> A. Well, that is all I can remember of it.
>
> Q. Do you recall what you did next in connection with the cottonseed oil futures market?
>
> A. Yes, sir, I picked up the telephone and I called Mr. Alex Caldwell in Washington, who was the head of the Commodity Exchange Authority.
>
> Q. Had you known Mr. Caldwell prior to that?
>
> A. For many years.
>
> Q. Did you speak with Mr. Caldwell?
>
> A. Yes.
>
> Q. As best you can recall, what did you say to Mr. Caldwell and what did he say to you
>
> A. I said, "Alex, what the devil do you do with a market where one interest has 90 per cent of the

> long side?" And he said, "Well, this is a tough question, I have never been faced with quite that situation before." He said, "It could come to the point where you have to liquidate the market at a fixed price, but", he said, "that is a very dangerous thing to do and could have bad implications not only for the Produce Exchange, but for all commodities markets in general." And I said, "Well, what do you think about the possibility of spreading this thing out by getting some other interest to take over the position of the long side? Liquidating it this way." And he said, "Well it certainly was worth exploring", and I asked him if there were more than one party involved in buying out this long position, whether it would give us anti-trust problems and he said that was not something he was competent to comment on. And I promised to keep him informed * * *.

A Special Meeting of the Board of the Produce Exchange was held the same afternoon. (Anderson, Tr. 3229, JA 1212a). There, Anderson reported on his conversation with Caldwell. (Anderson, Tr. 3235-3239, JA 1214a-1218a). After considerable discussion, the Board decided to appoint a small Control Committee to deal with the situation. (McDonald, Tr. 1670-1673, JA 567a-570a). Anderson was suggested for membership, but he declined to serve. (MacDonald, Tr. 1673-1675, JA 570a-572a; Berg, Tr. 2283, JA 828a; Fashena, Tr. 2568, JA 934a; Anderson, Tr. 3240, JA 1219a). As MacDonald testified, Anderson declined because he, Anderson, perceived a potential conflict of interest between the Control Committee and his position at Merrill Lynch, inasmuch as Merrill Lynch carried accounts for a number of customers who had open positions, both long and short, on the Produce Exchange and who might be asked by

the Control Committee to assume some of Allied's position as discussed by Anderson and Caldwell earlier that day. (MacDonald, Tr. 1673-1675, JA 570a-572a)*.

The prices on the Produce Exchange were quite stable on November 14. No panic had affected the market, which closed 19 points down out of a possible 200 point daily fluctuation limit on the Produce Exchange. (PX 156, JA 567e).

Friday, November 15

On Friday morning, November 15, 1963, Anderson received a telephone call from Caldwell of the CEA. Caldwell wanted to know what the Produce Exchange had decided to do. (Anderson, Tr. 3249, JA 1221a). Anderson informed him that the Board had met the previous day and had appointed a Control Committee. (Anderson Tr. 3249, JA 1221a). He advised Caldwell that he, Anderson, was not on the Control Committee and referred him to MacDonald, who was. (Anderson, Tr. 3249, JA 1221a).

The market declined a modest 15 points on November 15. (PX 156, JA 567e).

Monday, November 18

On Monday, November 18, 1963, after the close of the market, Anderson received a call from MacDonald, who recommended that the Produce Exchange impose a 25 point limit on daily price movements. (Anderson, Tr. 3252, JA 1223a). MacDonald advised Anderson that the narrower

* The minutes of the Special Meeting of November 14 erroneously recorded Anderson as being on the Control Committee. The minutes were corrected as soon as Anderson had occasion to note the error. (Tr. 3242, JA 1220a). There was no disagreement among the witnesses that Anderson was *not* on the Control Committee. (MacDonald, Tr. 1673-1675, JA 570a-572a; Berg, Tr. 2283, JA 828a; Fashena, Tr. 2568, JA 934a).

limit was necessary because Haupt, as he had just learned, was in net capital trouble with the New York Stock Exchange. (MacDonald, Tr. 1777-1778, JA 616a-617a; Anderson, Tr. 3252-3253, JA 1223a-1224a). Anderson then voted to impose the new limit along with other available members of the Executive Committee of the Board of the Produce Exchange. (MacDonald, Tr. 1777-1778, JA 616a-617a; Anderson, Tr. 3251-3252, JA 1222a-1223a). MacDonald's call that afternoon was the first inkling that Anderson had that Haupt had any financial problem and that it might be involved in the Allied situation. (Anderson, Tr. 3253, JA 1224a). Oddly, on the same day, the Chase Manhattan Bank, responding to Anderson's previous request for a credit check on Allied, informed the Merrill Lynch Credit Department that Allied's credit was "excellent". (Anderson, Tr. 3334, JA 1270a).

On November 18, the price of cottonseed oil futures contracts had declined an average of 100 points, its steepest decline during the entire post-November 14 period. (Ellison, Tr. 5217-5218, JA 1811a-1812a).

Tuesday, November 19

Tuesday, November 19, turned out to be a most hectic day. Upon arriving at work that morning, Anderson was asked to come "post haste" to the office of Michael McCarthy, chairman of the board of directors of Merrill Lynch. (Anderson, Tr. 3256, JA 1226a). In McCarthy's office were two of Haupt's general partners, Teiger and Brenner, who had come to Merrill Lynch for help at the suggestion of the New York Stock Exchange. (Anderson, Tr. 3256, JA 1226a). It was in McCarthy's office that morning that Anderson learned for the first time that Haupt was carrying virtually the entire Allied position on both the Produce Exchange and the Board of Trade in Chicago (Anderson, Tr. 3257, JA

1227a), and that, in addition, Haupt had lent heavily to Allied on the basis of warehouse receipts. (Anderson, Tr. 3257, JA 1227a). This was totally unprecedented news. While Anderson had known since November 14 that Allied held 90% of the open interest on the Produce Exchange, he had assumed that Allied's vast position was spread over ten to fifteen brokerage houses. (Anderson, Tr. 3258, JA 1228a).* He could not believe that one house would be so foolhardy and reckless as to assume the risk of so large a position. (Anderson, Tr. 3257-3258, JA 1227a-1228a). Teiger and Brenner advised Anderson and McCarthy that Allied had not been responding to Haupt's margin calls and that Haupt was fearful of running out of funds to pay the Clearing Association should the market continue to decline. (Anderson, Tr. 3257, JA 1227a).

In response to Haupt's call for help, Anderson agreed to contact a number of "cash houses", traders and crushers, which were also Merrill Lynch customers, to request them to take over all or part of Haupt's open position in cottonseed oil or soybean oil. (Anderson, Tr. 3258-3259, JA 1228a-1229a). The Haupt partners did not, at that point, wish to liquidate the contracts on the open market for fear of depressing prices further and they specifically asked Anderson to contact "cash houses" to take the positions over. (Anderson, Tr. 3259, 3342, JA 1229a, 1273a). Anderson took pains to clear this unorthodox procedure with the CEA. (Anderson, Tr. 3269, JA 1240a). He then called Proctor & Gamble, Anderson, Clayton & Co., Lever Brothers, Continental, Cooke & Co. (Anderson, Tr. 3260, JA 1230a).

With these calls outstanding, Anderson left to attend a special meeting of the New York Produce Exchange

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* The rule of thumb on the Street was that no one brokerage firm would carry more than 5% to 10% of the open interest for any one customer. (Barton, Tr. 5429-5431, JA 1868a-1870a).

Clearing Association to which he had been invited as a director-elect of its board of directors. (Boyer, Tr. 1213, JA 459a; Anderson, Tr. 3255, JA 1225a). He was scheduled to become a director in December of 1963. (Boyer, Tr. 1213, JA 459a). The meeting was called to consider the emergency in the cottonseed futures market which was now fast developing.

After the meeting at the Clearing Association, Anderson returned to his office, where he found a telephone message from an attorney for Bunge. (Anderson, Tr. 3261, JA 1232a). He returned the call and was informed that Bunge had a customer (not identified to Anderson) for whom it was carrying long positions in soybean oil and cottonseed oil futures contracts and that Bunge's customer had failed to respond to margin calls. (Anderson, Tr. 3262, JA 1233a). The Bunge attorney asked Merrill Lynch to liquidate these contracts. (Anderson, Tr. 3262, JA 1233a). Anderson told him that the Produce Exchange was "limit down" at that time, and, thus, the cottonseed oil contracts could not be sold, but that he would, however, relay Bunge's order to sell the soybean oil contracts on the Board of Trade in Chicago. (Anderson, Tr. 3262, JA 1233a).

Anderson then returned to McCarthy's office where he again met with Teiger and Brenner. (Anderson, Tr. 3262, JA 1233a). Since no positive responses had come in as yet from the Merrill Lynch customers which Anderson had called earlier, he suggested to Teiger and Brenner that Haupt at least try to liquidate Allied's soybean oil position on the Board of Trade, which was not "down the limit". (Anderson, Tr. 3262, JA 1233a). Teiger and Brenner agreed and asked Merrill Lynch to act as Haupt's broker. Anderson, however, declined, informing them that Merrill Lynch had a pending order (from Bunge) which had not yet been executed and which would be competing with Haupt's and

that Haupt should, therefore, ask another broker to execute its order. (Anderson, Tr. 3263, 3342, JA 1234a, 1273a). Anderson then contacted Bache & Co., the second largest commodities broker, which did arrange for the sale. (Anderson, Tr. 3263-3264, JA 1234a-1235a). By declining Haupt's order, Anderson waived an opportunity for Merrill Lynch to earn some $100,000 in commissions. (Anderson, Tr. 3321-3322, JA 1257a-1258a).

In the late afternoon of November 19, Anderson attended a special joint meeting of the respective Boards of the Produce Exchange and the Clearing Association. (Anderson, Tr. 3264-3265, JA 1235a-1236a). While this meeting was in progress it was announced that Allied had filed in bankruptcy. (Boyer, Tr. 1297, JA 473a; Fashena, Tr. 2575, JA 936a). Present at this joint meeting were, among others, two partners from Haupt, Kammerman (Haupt's managing partner) and Kaufman. (Anderson, Tr. 3265-3266, JA 1236a-1237a). Kammerman informed the meeting that if the market continued to decline Haupt would be unable to make further margin payments to the Clearing Association, but that if the Produce Exchange closed its market at a tolerable level, then Haupt would recover sufficient funds from the Clearing Association and would survive. (Anderson, Tr. 3266-3267, JA 1237a-1238a). The entire situation was discussed and various options considered. (Anderson, Tr. 3266, JA 1237a). Anderson mentioned that he had that day canvassed Merrill Lynch customers and found no interest by anyone in taking over Allied's position. (Fashena, Tr. 2662, JA 988a; Anderson, Tr. 3267-3268, JA 1238a-1239a). In sum, it was now known that Allied was insolvent, that Haupt was carrying virtually all of Allied's position, that Haupt was running into financial trouble and that Allied's position with Haupt could not be "spread". This constellation of facts was not known

before November 19. (Anderson, Tr. 3257-3259, JA 1227a-1229a).

It was thus decided to close the market and to settle outstanding contracts at a fair price. (Anderson, Tr. 3266, 3268, JA 1237a, 1239a). Anderson, and others present at the meeting, including Kammerman and Kaufman, thought that Haupt had been saved from bankruptcy. To keep the market open would have spelled the certain doom of Haupt not only as a commodities house but also as a New York Stock Exchange member firm with many public customers. Kammerman and Kaufman stayed until after the settlement price had been worked out (Anderson, Tr. 3267, JA 1238a) and until they were assured that Haupt would receive over three million dollars from the Clearing Association. (Berg, Tr. 2296, JA 831a). Subsequently, Brenner, one of the Haupt partners who had met earlier that day with Anderson at Merrill Lynch, went out of his way to personally thank the Produce Exchange for its courageous action. (MacDonald, Tr. 1875, JA 657a; Fashena, Tr. 2659, JA 987a; DX 106, JA 1111e).

Much later, after November 20, 1963, it was discovered that the American Express warehouse receipts given by Allied as collateral to Haupt were fraudulent and that Allied's oil tanks contained only greasy water. (DeAngelis, Tr. 2979, JA 1121a). With its collateral worthless, Haupt collapsed and was declared a bankrupt.

The Role of Merrill Lynch

Little need be added to describe Merrill Lynch's involvement in the events of 1963. In both Counts I and II the Trustee alleges that, for the periods prior and subsequent to November 14, Anderson's "failure to regulate" should

be imputed to Merrill Lynch and that Merrill Lynch and Anderson were part of a conspiracy against Haupt in violation of the anti-trust laws. The alleged basis for such vicarious liability is that Anderson's actions or inactions as a "regulator" were in bad faith and within the scope of his employment at Merrill Lynch.

The Trustee, however, failed to adduce any evidence to support his theories and the District Court properly directed a verdict in favor of Merrill Lynch. Indeed, the Trustee's evidentiary failure at trial was no surprise. Earlier, at the time of Merrill Lynch's motion for summary judgment, the District Court had already observed the Trustee's lack of proof after years of pre-trial discovery. *Seligson* v. *New York Produce Exchange,* 378 F. Supp. 1076, 1089 (S.D.N.Y. 1974).

> [Trustee's] chances for success at trial, even at the directed verdict stage, are diminished somewhat by the fact that Merrill Lynch neither had a business relationship with Allied, nor traded on the Exchange for its own account, nor in any other way appears to have had a direct interest in how the Exchange was regulated.

The Trustee's utter failure of proof was made crystal clear at trial, leading to the direction of a verdict by the District Court.

CONCLUSION

The judgment below should be affirmed in all respects.

Dated: New York, N. Y.
June 11, 1976

Respectfully submitted,

BROWN, WOOD, IVEY, MITCHELL & PETTY
Attorneys for Defendants-Appellees
Harry B. Anderson and Merrill Lynch,
Pierce, Fenner & Smith Incorporated
One Liberty Plaza
New York, N. Y. 10006
(212) 349-7500

Of Counsel:
HENRY F. MINNEROP
DUNCAN N. DARROW

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8-6- 1976

PAUL, WEISS, RIFKIND, WHARTON & GARRISON

By Clare A. Kocco

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WEIL, GOTSHAL & MANGES

Attorneys for Harvey Muller

Date: 8/6/76 3:30 pm

(2) COPY RECEIVED

J.NINE, CONNELLY, CHASE, O'DONNELL & WEYHER

Attorneys for NYPE, MACDONALD, PASNCWA, I. USISR

Date 8/6/76 3:55 pm

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BIVET, BALLANTINE, BUSHBY, PALMER & WOOD

Attorneys For: Bunge - Walter C Klein